

Decision **PROPOSED DECISION OF COMMISSIONER SANDOVAL**
(Mailed 1/11/2013)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking into the
Review of the California High Cost
Fund-A Program.

Rulemaking 11-11-007
(Filed November 10, 2011)

**INTERIM DECISION ADOPTING A ONE-YEAR FREEZE IN GENERAL RATE
CASE SCHEDULES AND WATERFALL PROVISIONS FOR CALIFORNIA
HIGH COST FUND-A RECIPIENTS****Summary**

This interim decision implements a one-year freeze in the general rate case schedules and waterfall provisions for California High Cost Fund-A recipients. The freeze can be extended for six months by a ruling of the assigned Administrative Law Judge if this proceeding is not completed by December 31, 2013.

This proceeding remains open.

1. Background and Relevant Procedural History

With the Order Instituting Rulemaking (OIR) (Rulemaking (R.) 11-11-007), the Commission began a review of the California High Cost Fund-A (CHCF-A) program. The OIR was issued pursuant to the Commission's Decision (D.) 10-02-016. The Commission has determined that a detailed review of the program is warranted in response to market, regulatory, and technological changes since the CHCF-A program was first established in 1987. In this OIR, the Commission seeks comment on how the program can more efficiently and

effectively meet its stated goals. To the extent deficiencies are identified, the Commission will solicit constructive proposals on whether the program should continue and if so, how should it be modified.

The CHCF-A rules are summarized in Appendix, Section D to D.91-09-042. Pursuant to these rules Small Local Exchange Carriers wishing to receive CHCF-A support must periodically file General Rate Cases (GRCs) with the Commission. Under this procedure recipients of CHCF-A subsidies are subject to a six-year phase-down cycle. The cycle begins on January 1 after a GRC decision is issued. A company receives full (100%) funding for three years following the GRC decision. In the fourth year the company receives funding at 80% of the GRC decision; in the fifth year 50% and in the sixth year 0%, unless a new rate case is filed. The cycle begins again with the filing and approval of a GRC application. This six-year cycle with reduced funding levels after three years is referred to as the “waterfall.” GRCs are only required to be filed by CHCF-A eligible companies who wish to avail themselves of the A-fund subsidies.

The OIR was approved on November 10, 2011, and issued on November 18, 2011. The preliminary schedule mandated that the initial comments be filed and served 61 days after issuance (January 18, 2012),¹ and that reply comments be due 91 days after issuance. In a ruling issued on January 17, a request for extension was granted. By that ruling, the proceeding schedule was revised so that initial comments were to be filed and served by February 1, and reply comments were to be filed and served by March 2.

¹ All dates are 2012 unless otherwise noted.

On January 18 the Commission's Division of Ratepayer Advocates (DRA) filed a Motion to Freeze the 2012 "Waterfall" Provisions of the California High Cost Fund-A; Stay Application (A.) 11-12-011 of Kerman Telephone Company and Suspend Processing of all A-Fund Company Applications for Review of Rates, Charges and Rates of Return. In an e-mail ruling issued on January 23, the assigned Administrative Law Judge (ALJ) denied the request to stay A.11-12-011 (Kerman) as the request was more properly considered by the assigned ALJ in that proceeding. Parties were given until February 2 to respond to the portions of DRA's Motion regarding the freeze of the waterfall provisions of the CHCF-A and suspension of processing of all A-Fund company applications (with the exception of A.11-12-011).

On February 2, Calaveras Telephone Company, Cal-Ore Telephone Company, Ducor Telephone Company, Foresthill Telephone Company, Kerman Telephone Company, Pinnacles Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Inc., The Siskiyou Telephone Company and Volcano Telephone Company (collectively, Small Local Exchange Carriers (LECs) or Incumbent Local Exchange Carriers (ILECs)) filed a response in opposition to the DRA's motion to freeze. On February 13, DRA filed a reply to the response.

On June 4, a prehearing conference (PHC) was held in the instant proceeding. The assigned Commissioner and the assigned ALJ were both present at the hearing. The assigned ALJ indicated that he could not address

DRA's motion to freeze in a ruling, that it was for the Commission to decide whether to freeze the pending GRCs of the Small ILECs.²

On October 13 counsel for the Small ILECs sent a letter to the Commission's Executive Director requesting a 90-day extension of time of the January 1, 2013 deadline for CHCF-A recipients to file a rate case to prevent operation of the "waterfall" mechanism, as required by D.91-09-042, Section D of the Appendix. The letter requested that the extension of time be granted until April 1, 2013. In a letter dated October 22, the Executive Director granted the request for a 90-day extension.

On October 15, the Small ILECs filed a motion for a Proposed Decision adopting a one-year freeze in the CHCF-A Rate Case Schedule and "Waterfall Mechanism." On October 30 DRA, The Utility Reform Network (TURN) and other parties filed responses to the Small ILECs' motion. The assigned ALJ allowed the Small ILECs to file a Reply to the Responses, which was done on November 5, 2012.

2. Proposed GRC and Waterfall Rate Freeze

Both DRA and the Small ILECs agree that there should be some type of freeze on the CHCF-A rate case schedule and waterfall mechanism. DRA states that it requests a freeze so that A-Fund companies, parties to the proceeding, and Commission staff can focus their efforts on responding to and addressing the questions and issues presented by the OIR.³ DRA argues that without the requested freeze parties will be forced to simultaneously provide information

² PHC Transcript 10:12-22.

³ DRA Motion to Freeze at 1.

and recommendations to the Commission in the instant proceeding while litigating the Small ILECs' GRC applications.⁴ DRA contends it makes little sense to process the GRCs necessary to reset a company's A-fund subsidy at the same time the A-Fund rules are under review and subject to possible revision.⁵

DRA has recommended a two-pronged approach to resolving the conflict between the instant OIR and pending GRCs. First, the Commission should suspend the processing of all the Small ILECs' GRC applications during the pendency of the instant OIR.⁶ Second, the Commission should freeze the "waterfall" subsidy percentage for the Small ILEC at their current levels. The suspension and freeze would remain in place until the Commission issues a final decision in this proceeding.⁷

In their February response the Small ILECs opposed DRA's motion in total; however, since they have now made a freeze proposal of their own we will focus on the Small ILECs' opposition to the DRA motion contained in their motion to freeze and reply to responses to the their motion to freeze. Two of the Small ILECs' objections are no longer relevant. The first objection was over inclusion of the Kerman proceeding in the DRA freeze motion. As previously noted, the assigned ALJ (in an e-mail ruling) has denied that portion of the motion. Secondly, the Small ILECs objected to the DRA motion seeking a ruling from the assigned ALJ instead of a Commission vote. As noted above, the assigned ALJ has indicated that the freeze motion is more properly considered

⁴ *Id.*

⁵ *Id.*

⁶ *Id.* at 2.

⁷ *Id.* at 3.

by the full Commission as it is a request *to* modify the GRC cycle set forth in D.91-09-042, and thus requires explicit Commission approval. The Small ILECs have also argued that the Commission “cannot lawfully” prevent them from filing rate cases without their agreement.⁸ The Small ILECs contend that, absent their agreement, a freeze would be an arbitrary and capricious administrative action that could effectuate an unconstitutional taking of utility property.⁹

The Small ILECs have proposed a one-year stay in the general current rate case schedule. Their proposal has five components; 1) No new GRCs would be filed by the Small ILECs (with the exception of Kerman) until December 1, 2013;¹⁰ 2) The waterfall provisions of D.91-09-042 would be suspended for one year at the current CHCF-A subsidy level for the Small ILECs (with the exception of Kerman);¹¹ 3) All other features of the current CHCF-A program would remain in effect during the proposed freeze; 4) The Small ILECs would retain the ability to file an application for emergency rate relief;¹² and 5) In September 2013 the Small ILECs and the other parties to the proceeding would confer in order to determine if a further stay/freeze in the GRC and waterfall were warranted.¹³

DRA has urged the Commission to reject the Small ILECs’ motion and grant DRA’s motion.¹⁴ DRA argues that its freeze proposal provides an efficient

⁸ Small ILECs’ Motion to Freeze at 6:1-8.

⁹ *Id.*

¹⁰ *Id.* 1:17-18.

¹¹ *Id.* 1:20-22.

¹² Reply of Small ILECs to Responses to Motion for Freeze, 3:3-6.

¹³ Small ILECs’ Motion to Freeze, 2:1-3.

¹⁴ DRA Response to Small ILECs’ motion to Freeze at 2.

and orderly path to examine the issues in the instant proceeding.¹⁵ If the Small ILECs' motion is approved, DRA requests that the Commission include an automatic six month extension of the stay/freeze if the proceeding is not completed by December 31, 2013.¹⁶

TURN states that in general it is not opposed to the Small ILECs' (or DRA's) motion to freeze but that the "devil is in the details."¹⁷ TURN indicates that a freeze lasting until the proceeding is concluded (DRA's proposal) is likely more efficient than the Small ILECs' freeze proposal.¹⁸ TURN has expressed concern with the emergency rate relief provision in the Small ILECs' motion. They view the provision as being unbalanced and overly protective of the interests of the Small ILECs.¹⁹ TURN argues that the Commission has several mechanisms for regulated utilities to request different types of relief, including advice letters, applications, motions, and requests to the Executive Director.²⁰ DRA has raised similar concerns about the Small ILECs' emergency relief provision. The Small ILECs have revised the emergency rate relief provision in response to TURN's and DRA's concerns.²¹

Happy Valley Telephone Company (U1010C), Hornitos Telephone Company (U1011C) and Winterhaven Telephone Company (U1021C)

¹⁵ *Id.* at 3.

¹⁶ *Id.* at 4.

¹⁷ TURN's Response to Small ILECs' motion to Freeze at 1.

¹⁸ *Id.*

¹⁹ TURN's Response to Small ILECs' motion to Freeze at 2.

²⁰ *Id.* at 3.

²¹ Small ILEC's reply to response to motion to Freeze, 3:1-6.

(collectively, TDS Telecom) do not object to the Small ILECs' motion to freeze as long as it applies only to the Small ILECs.²² TDS does object to any decision that would impose a stay or freeze on them.²³

3. Discussion

There is a basic consensus that a stay in the Small ILECs' pending GRC applications and a freeze of the CHCF-A waterfall provisions are warranted. The parties differ on whether the stay should be for one year, with a status review after nine months, or remain in place until the proceeding is concluded. TURN makes a valid point that DRA's proposal is likely the more efficient. However, the Small ILECs' contend that a freeze lasting more than a year would be both unreasonable and unlawful. We acknowledge their first point and disagree with the second.

DRA urges the Commission to reject the Small ILECs' motion in favor of its own. If the Commission does adopt the Small ILECs' motion, DRA urges the Commission to include an automatic six month extension if the OIR is not concluded by December 31, 2013.

It is unlikely that the instant proceeding will be concluded by December 2013. All parties agree that some type of freeze is warranted. We conclude that a one year stay of the Small ILECs' pending GRC proceedings, with the exception of the Kerman GRC (A.11-12-011)²⁴ is in the public interest, along with a one-year freeze in the CHCF-A waterfall provisions at their current levels. The parties

²² TDS Telecom response to motion to Freeze 2:12-14.

²³ *Id.*

²⁴ Kerman's GRC request will be addressed in A.11-12-011.

will review that status of the proceeding in September of 2013. If it appears that the proceeding will not be concluded by December 31, 2013, any party may request an extension of the freeze for an additional six months. The extension request may be approved or rejected by a ruling of the assigned ALJ, pursuant to Rule 11.1. If an extension is granted, the parties will again review the status of the proceeding in March 2014. If it appears that the proceeding will not be concluded by June 30, 2014, any party may again request a six-month extension, until December 31, 2014. The second request must be acted on by a Commission decision.

DRA's Motion to Freeze the 2012 "Waterfall" Provisions of the California High Cost Fund-A; Stay Application (A.) 11-12-011 of Kerman Telephone Company and Suspend Processing of all A-Fund Company Applications for Review of Rates, Charges and Rates of Return is denied. The Small ILECs' Motion for a Proposed Decision adopting a one-year freeze in the CHCF-A Rate Case Schedule and "Waterfall Mechanism" is approved as modified consistent with the above.

4. Categorization and Need for Hearings

The Commission preliminarily categorized this rulemaking to be "quasi-legislative" and preliminarily determined that hearings are unnecessary. The final determination of whether a public hearing is necessary will be made at a later date. The designation of quasi-legislative remains.

5. Comments on Proposed Decision

The proposed decision of the Commissioner in this matter was mailed to the parties in accordance with Section 311 of the Public Utilities Code and comments were allowed under Rule 14.3 of the Commission's Rules of Practice and Procedure. Comments were filed on January 31, 2013 by the Small ILECs,

DRA and TDS Telecom and reply comments were filed on February 5, 2013 by DRA and the Small ILECs.

In their opening comments, the Small ILECs support the one-year freeze and stay but state that the proposed decision (PD) should be revised in order to: 1) Clarify that the stay is retroactive to January 1, 2013 and will last until December 31, 2013, 2) Revise Ordering Paragraph 4 to remove the term “at their current levels” as it could be interrupted to undercut the annual CHCF-A Fund adjustment process, and 3) Remove the statement in the OIR that “the Commission will solicit constructive proposals on whether the program should continue” as it is inconsistent with the current statute. In addition the Small ILECs reserve the right to oppose a stay longer than one year and they affirmatively oppose the provision in the PD that allows the assigned ALJ to extend the stay by six months. The Small ILECs argue that the extension provision is a violation of their due process rights and, to the extent that they are earning less than their authorized rate of return, an unlawful and unconstitutional taking of property.

In their opening comments TDS does not object to the stay, as set forth in the PD, as it would expressly not apply to them. However, like the Small ILECs, TDS objects to the statement in the OIR that “the Commission will solicit constructive proposals on whether the program should continue” as it is, allegedly, inconsistent with the current statute.²⁵

In their opening comments DRA generally supports the PD but suggests modifications regarding the standard of review for requests for interim or

²⁵ TDS and the Small ILECs have neglected to note that the relevant statute, SB 379, expires on January 1, 2015.

emergency rate relief during the proceeding. DRA argues that the Small ILECs' ability to seek emergency rate relief should be subject to detailed scrutiny by the Commission and bear a heavy burden of proof.

In their reply comments, DRA addresses the Small ILECs' assertions that the Commission is precluded from adopting a stay of the GRC and waterfall mechanism for longer than one year and that the assigned ALJ does not have the authority to grant a temporary six-month extension of the stay. DRA states that the Fifth Amendment to the U.S. Constitution provides just compensation for private property that is taken for public use. DRA argues that the CHCF-A is a subsidy from California rate payers to the Small ILECs and that ratepayer funds are not the ILECs private property. DRA asserts that the Small ILECs do not have a fundamental right to the funds. DRA points out that the PD does not change the Small ILECs' current rates or take away any subsidy. DRA, also, argues that allowing the assigned ALJ to grant a six-month extension of the freeze is not a violation of Commission rules or statute. Finally, DRA does not oppose the Small ILECs' ability to make annual CHCF-A Fund adjustment filings but does oppose any adjustments that would include rate case expenses.

In their reply comments the Small ILECs argue that the Commission should adopt the PD subject to the suggested modifications raised in their opening comments.

We have reviewed the opening and reply comments submitted in response to the instant Interim PD. A Conclusion of Law (#3) and an Ordering Paragraph (#7) have been added to clarify that the freeze runs from January 1, 2013 to and including December 31, 2013, unless a further extension is granted and the other Conclusions of Law and Ordering Paragraphs renumbered as appropriate. Ordering Paragraph 4 has been modified to explicitly allow the Small ILECs to

make annual A-Fund adjustment filings. All other comments seeking changes to the PD are denied.

6. Assignment of Proceeding

Catherine J.K. Sandoval is the assigned Commissioner and Presiding Officer and W. Anthony Colbert is the assigned ALJ in this proceeding.

Findings of Fact

1. The OIR was issued pursuant to the Commission's D.10-02-016.
2. The OIR (R.11-11-007) begins a review of the CHCF-A program.
3. The CHCF-A rules are summarized in Appendix, Section D to D.91-09-042.
4. Small LEC wishing to receive CHCF-A support must periodically file GRCs with the Commission.
5. CHCF-A subsidies are subject to a six-year phase down cycle or “waterfall.”
6. A company receives full (100%) funding for three years following the GRC decision.
7. In the fourth year the company would receive funding at 80% of the GRC decision; in the fifth year 50% and in the sixth year 0% unless a new rate case is filed
8. On January 18, 2012, DRA filed a Motion to Freeze the 2012 “Waterfall” Provisions of the California High Cost Fund-A and Suspend Processing of all A-Fund Company GRC Applications.
9. The Small ILECs have proposed a one-year stay in the general current rate case schedule and one year freeze of the waterfall provisions.
10. The Small ILECs propose that no new GRCs would be filed by the Small ILECs (with the exception of Kerman) until December 1, 2013.

11. The Small ILECs propose that the waterfall provisions of D.91-09-042 would be suspended for one year at the current CHCF-A subsidy level for the Small ILECs (with the exception of Kerman) and that all other features of the current CHCF-A program would remain in effect during the proposed freeze. The Small ILECs would retain the ability to file an application for emergency rate relief.

12. In September 2013 the Small ILECs and the other parties to the proceeding would confer in order to determine if a further stay/freeze in the GRC and waterfall were warranted.

13. It is unlikely that the instant proceeding will be concluded by December 2013.

14. A one-year stay of the Small ILEC's pending GRC proceedings along with a one-year freeze in the CHCF-A waterfall provisions at their current levels (with the exception of Kerman) are warranted.

Conclusions of Law

1. DRA's Motion to Freeze the 2012 "Waterfall" Provisions of the California High Cost Fund-A; Stay Application (A.) 11-12-011 of Kerman Telephone Company and Suspend Processing of all A-Fund Company Applications for Review of Rates, Charges and Rates of Return should be denied.

2. The Small ILECs' Motion for a PD adopting a one-year freeze in the CHCF-A Rate Case Schedule and "Waterfall Mechanism" should be approved as long as it is modified to allow extensions of the freeze.

3. The one-year freeze in the CHCF-A Rate Case Schedule and "Waterfall Mechanism" should be retroactive to January 1, 2013 and extend to and including December 31, 2013 unless a further extension is granted.

4. All other features of the current CHCF-A program should remain in effect during the proposed stay and freeze.

5. The Small ILECs should retain the ability to file an application for emergency rate relief through the existing Commission process.

6. The parties should confer to review that status of the instant proceeding in September of 2013.

7. If it appears that the proceeding will not be concluded by December 31, 2013, any party may request an extension of the freeze for an additional six months.

8. The assigned ALJ may approve or reject the extension request.

9. If an extension is granted, by the assigned ALJ, the parties should again confer to review the status of the instant proceeding in March 2014.

10. If it appears that the proceeding will not be concluded by June 30, 2014, any party may request a second six-month extension, until December 31, 2014, which must be considered by the full Commission.

O R D E R

IT IS ORDERED that:

1. The Motion of the Commission's Division of Ratepayer Advocates to Freeze the 2012 "Waterfall" Provisions of the California High Cost Fund-A; Stay Application 11-12-011 of Kerman Telephone Company and Suspend Processing of all California High Cost Fund-A Company Applications for Review of Rates, Charges and Rates of Return is denied.

2. The Motion of Calaveras Telephone Company, Cal-Ore Telephone Company, Ducor Telephone Company, Foresthill Telephone Company,

Pinnacles Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Inc., The Siskiyou Telephone Company and Volcano Telephone Company (collectively, Small Local Exchange Carriers or Incumbent Local Exchange Carriers) for a Proposed Decision adopting a one year freeze in the California High Cost Fund-A Rate Case Schedule and “Waterfall Mechanism” is approved as modified by and consistent with Ordering Paragraphs 7, 8, 9 and 10 of this decision.

3. The General Rate Case proceedings of Calaveras Telephone Company, Cal-Ore Telephone Company, Ducor Telephone Company, Foresthill Telephone Company, Pinnacles Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Inc., The Siskiyou Telephone Company and Volcano Telephone Company will be stayed for one year.

4. The “Waterfall Provisions” of the California High Cost Fund-A will be frozen for one year at their current levels for Calaveras Telephone Company, Cal-Ore Telephone Company, Ducor Telephone Company, Foresthill Telephone Company, Pinnacles Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Inc., The Siskiyou Telephone Company and Volcano Telephone Company subject to any adjustments in funding that result from the California High Cost Fund-A annual filings.

5. All other features of the current California High Cost Fund-A program will remain in effect during the proposed stay and freeze.

6. Calaveras Telephone Company, Cal-Ore Telephone Company, Ducor Telephone Company, Foresthill Telephone Company, Pinnacles Telephone Company, The Ponderosa Telephone Company, Sierra Telephone Company, Inc., The Siskiyou Telephone Company and Volcano Telephone Company will retain

the ability to file an application for emergency rate relief through the existing Commission process.

7. The one-year freeze in the California High Cost Fund-A Rate Case Schedule and “Waterfall Mechanism” is retroactive to January 1, 2013 and extends to and including December 31, 2013 unless a further extension is granted.

8. The parties to this proceeding will confer to review that status of the proceeding in September 2013. If it appears that the proceeding will not be concluded by December 31, 2013, any party may request an extension of the stay and freeze for an additional six months. The extension request will be approved or rejected by a ruling of the assigned Administrative Law Judge.

9. If an extension is granted by the assigned Administrative Law Judge, the parties will confer to review the status of the proceeding in March 2014. If it appears that the proceeding will not be concluded by June 30, 2014, any party may request a six month extension, until December 31, 2014.

10. The second request for an extension of the stay and freeze must be considered by the full Commission.

11. Rulemaking 11-11-007 remains open.

This order is effective today.

Dated _____, at San Francisco, California.